MICROSOFT CORP
Form 10-Q
October 24, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended September 30, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Transition Period From to

Commission File Number: 001-37845

MICROSOFT CORPORATION

(Exact name of registrant as specified in its charter)

Washington	91-1144442
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
One Microsoft Way, Redmond, Washington	98052-6399
(Address of principal executive offices)	(Zip Code)

(425) 882-8080

(Registrant's telephone number, including area code)

None

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
Emerging growth company	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding as of October 19, 2018
Common Stock, $0.00000625 par value per share	7,676,218,736 shares

MICROSOFT CORPORATION

FORM 10-Q

For the Quarter Ended September 30, 2018

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

INCOME STATEMENTS

(In millions, except per share amounts) (Unaudited)

Three Months Ended September 30,	2018	2017
Revenue:		
Product	$ 17,299	$14,298
Service and other	11,785	10,240
Total revenue	29,084	24,538
Cost of revenue:		
Product	3,649	2,980
Service and other	6,256	5,298
Total cost of revenue	9,905	8,278
Gross margin	19,179	16,260
Research and development	3,977	3,574
Sales and marketing	4,098	3,812
General and administrative	1,149	1,166
Operating income	9,955	7,708
Other income, net	266	276
Income before income taxes	10,221	7,984
Provision for income taxes	1,397	1,408
Net income	$8,824	$6,576

Earnings per share:		
Basic	$1.15	$0.85
Diluted	$1.14	$0.84
Weighted average shares outstanding:		
Basic	7,673	7,708
Diluted	7,766	7,799
Cash dividends declared per common share	$0.46	$0.42

Refer to accompanying notes.

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COMPREHENSIVE INCOME STATEMENTS

(In millions) (Unaudited)

Three Months Ended September 30,	2018	2017
Net income	$ 8,824	$ 6,576
Other comprehensive income (loss), net of tax:		
Net change related to derivatives	(45)	(106)
Net change related to investments	(261)	(288)
Translation adjustments and other	(55)	293
Other comprehensive loss	(361)	(101)
Comprehensive income	$ 8,463	$ 6,475

Refer to accompanying notes. Refer to Note 16 – Accumulated Other Comprehensive Income (Loss) for further information.

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BALANCE SHEETS

(In millions) (Unaudited)

	September 30, 2018	June 30, 2018
Assets		
Current assets:		
Cash and cash equivalents	$ 15,137	$ 11,946
Short-term investments	120,743	121,822
Total cash, cash equivalents, and short-term investments	135,880	133,768
Accounts receivable, net of allowance for doubtful accounts of $319 and $377	17,390	26,481
Inventories	3,614	2,662
Other	7,311	6,751
Total current assets	164,195	169,662
Property and equipment, net of accumulated depreciation of $30,953 and $29,223	31,430	29,460
Operating lease right-of-use assets	6,734	6,686
Equity investments	2,034	1,862
Goodwill	35,855	35,683
Intangible assets, net	7,579	8,053
Other long-term assets	9,792	7,442
Total assets	$ 257,619	$ 258,848
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$ 8,511	$ 8,617
Current portion of long-term debt	6,497	3,998
Accrued compensation	4,271	6,103
Short-term income taxes	2,341	2,121
Short-term unearned revenue	26,704	28,905
Other	7,953	8,744
Total current liabilities	56,277	58,488

Long-term debt	69,733	72,242
Long-term income taxes	28,936	30,265
Long-term unearned revenue	3,538	3,815
Deferred income taxes	1,977	541
Operating lease liabilities	5,652	5,568
Other long-term liabilities	5,539	5,211
Total liabilities	171,652	176,130
Commitments and contingencies		
Stockholders' equity:		
Common stock and paid-in capital – shares authorized 24,000; outstanding 7,680 and 7,677	71,303	71,223
Retained earnings	17,279	13,682
Accumulated other comprehensive loss	(2,615)	(2,187)
Total stockholders' equity	85,967	82,718
Total liabilities and stockholders' equity	$ 257,619	$258,848

Refer to accompanying notes.

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CASH FLOWS STATEMENTS

(In millions) (Unaudited)

Three Months Ended September 30,	2018	2017
Operations		
Net income	$8,824	$6,576
Adjustments to reconcile net income to net cash from operations:		
Depreciation, amortization, and other	2,837	2,499
Stock-based compensation expense	1,107	973
Net recognized gains on investments and derivatives	(240)	(523)
Deferred income taxes	(247)	(53)
Changes in operating assets and liabilities:		
Accounts receivable	9,194	7,949
Inventories	(956)	(1,023)
Other current assets	(677)	(318)
Other long-term assets	21	(278)
Accounts payable	(395)	(407)
Unearned revenue	(2,441)	(1,806)
Income taxes	(1,091)	661
Other current liabilities	(2,322)	(2,164)
Other long-term liabilities	43	354
Net cash from operations	13,657	12,440
Financing		
Repayments of short-term debt, maturities of 90 days or less, net	0	(3,710)
Proceeds from issuance of debt	0	3,954
Repayments of debt	0	(1,169)
Common stock issued	360	307
Common stock repurchased	(3,744)	(2,570)
Common stock cash dividends paid	(3,220)	(3,003)
Other, net	(780)	(150)
Net cash used in financing	(7,384)	(6,341)

Investing

Additions to property and equipment	(3,602)	(2,132)
Acquisition of companies, net of cash acquired, and purchases of intangible and other assets	(245)	(179)
Purchases of investments	(19,551)	(32,961)
Maturities of investments	5,214	5,226
Sales of investments	15,231	23,036
Securities lending payable	0	106
Net cash used in investing	(2,953)	(6,904)
Effect of foreign exchange rates on cash and cash equivalents	(129)	26
Net change in cash and cash equivalents	3,191	(779)
Cash and cash equivalents, beginning of period	11,946	7,663
Cash and cash equivalents, end of period	$15,137	$6,884

Refer to accompanying notes.

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STOCKHOLDERS’ EQUITY STATEMENTS

(In millions) (Unaudited)

Three Months Ended September 30,	2018	2017
Common stock and paid-in capital		
Balance, beginning of period	$71,223	$69,315
Common stock issued	360	307
Common stock repurchased	(1,387)	(1,175)
Stock-based compensation expense	1,107	973
Other, net	0	(1)
Balance, end of period	71,303	69,419
Retained earnings		
Balance, beginning of period	13,682	17,769
Net income	8,824	6,576
Common stock cash dividends	(3,528)	(3,239)
Common stock repurchased	(2,376)	(1,404)
Cumulative effect of accounting changes	677	0
Balance, end of period	17,279	19,702
Accumulated other comprehensive income (loss)		
Balance, beginning of period	(2,187)	627
Other comprehensive loss	(361)	(101)
Cumulative effect of accounting changes	(67)	0
Balance, end of period	(2,615)	526
Total stockholders’ equity	$85,967	$ 89,647

Refer to accompanying notes.

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NOTES TO FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 — ACCOUNTING POLICIES

Accounting Principles

Our unaudited interim consolidated financial statements and accompanying notes are prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). In the opinion of management, the unaudited interim consolidated financial statements reflect all adjustments of a normal recurring nature that are necessary for a fair presentation of the results for the interim periods presented. Interim results are not necessarily indicative of results for a full year. The information included in this Form 10-Q should be read in conjunction with information included in the Microsoft Corporation fiscal year 2018 Form 10-K filed with the U.S. Securities and Exchange Commission on August 3, 2018.

We have recast certain prior period amounts related to investments, derivatives, and fair value measurements to conform to the current period presentation based on our adoption of the new accounting standard for financial instruments. We have also recast prior period commercial cloud revenue to include the commercial portion of LinkedIn to provide a comparable view of our commercial cloud business performance. The commercial portion of LinkedIn includes LinkedIn Recruiter, Sales Navigator, premium business subscriptions, and other services for organizations. The recast of these prior period amounts had no impact on our consolidated financial statements.

Principles of Consolidation

The consolidated financial statements include the accounts of Microsoft Corporation and its subsidiaries. Intercompany transactions and balances have been eliminated.

Estimates and Assumptions

Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses. Examples of estimates and assumptions include: for revenue recognition, determining the nature and timing of satisfaction of performance obligations, and determining the standalone selling price of performance obligations, variable consideration, and other obligations such as product returns and refunds; loss contingencies; product warranties; the fair value of and/or potential impairment of goodwill and intangible assets for our reporting units; product life cycles; useful lives of our tangible and intangible assets; allowances for doubtful accounts; the market value of, and demand for, our inventory; stock-based compensation forfeiture rates; when technological feasibility is achieved for our products; the potential outcome of future tax consequences of events that have been recognized on our consolidated financial statements or tax returns; and determining the timing and amount of impairments for investments. Actual results and outcomes may differ from management’s estimates and assumptions.

Financial Instruments

Investments

We consider all highly liquid interest-earning investments with a maturity of three months or less at the date of purchase to be cash equivalents. The fair values of these investments approximate their carrying values. In general, investments with original maturities of greater than three months and remaining maturities of less than one year are classified as short-term investments. Investments with maturities beyond one year may be classified as short-term based on their highly liquid nature and because such marketable securities represent the investment of cash that is available for current operations.

Debt investments are classified as available-for-sale and realized gains and losses are recorded using the specific identification method. Changes in fair value, excluding other-than-temporary impairments, are recorded in other comprehensive income ("OCI"). Debt investments are impaired when a decline in fair value is judged to be other-than-temporary. Fair value is calculated based on publicly available market information or other estimates determined by management. We employ a systematic methodology on a quarterly basis that considers available quantitative and qualitative evidence in evaluating potential impairment of our investments. If the cost of an investment exceeds its fair value, we evaluate, among other factors, general market conditions, credit quality of debt instrument issuers, and the duration and extent to which the fair value is less than cost. We also evaluate whether we have plans to sell the security or it is more likely than not that we will be required to sell the security before recovery. In addition, we consider specific adverse conditions related to the financial health of and business outlook for the investee, including industry and sector performance, changes in technology, and operational and financing cash flow factors. Once a decline in fair value is determined to be other-than-temporary, an impairment charge is recorded in other income (expense), net and a new cost basis in the investment is established.

Equity investments with readily determinable fair values are measured at fair value. Equity investments without readily determinable fair values are measured using the equity method, or measured at cost with adjustments for observable changes in price or impairments (referred to as the measurement alternative). We perform a qualitative assessment on a quarterly basis and recognize an impairment if there are sufficient indicators that the fair value of the investment is less than carrying value. Changes in value are recorded in other income (expense), net.

We lend certain fixed-income and equity securities to increase investment returns. These transactions are accounted for as secured borrowings and the loaned securities continue to be carried as investments on our consolidated balance sheets. Cash and/or security interests are received as collateral for the loaned securities with the amount determined based upon the underlying security lent and the creditworthiness of the borrower. Cash received is recorded as an asset with a corresponding liability.

Derivatives

Derivative instruments are recognized as either assets or liabilities and are measured at fair value. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation.

For derivative instruments designated as fair value hedges, gains and losses are recognized in other income (expense), net with offsetting gains and losses on the hedged items. For options designated as fair value hedges, changes in the time value are excluded from the assessment of hedge effectiveness and recognized in other income (expense), net.

For derivative instruments designated as cash flow hedges, the effective portion of the gains and losses are initially reported as a component of OCI and subsequently recognized in revenue when the hedged exposure is recognized in revenue. Gains and losses on derivatives representing either hedge components excluded from the assessment of effectiveness or hedge ineffectiveness are recognized in other income (expense), net.

For derivative instruments that are not designated as hedges, gains and losses from changes in fair values are primarily recognized in other income (expense), net.

Fair Value Measurements

We account for certain assets and liabilities at fair value. The hierarchy below lists three levels of fair value based on the extent to which inputs used in measuring fair value are observable in the market. We categorize each of our fair value measurements in one of these three levels based on the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

- Level 1 – inputs are based upon unadjusted quoted prices for identical instruments in active markets. Our Level 1 investments primarily include U.S. government securities, common and preferred stock, and mutual funds. Our Level 1 derivative assets and liabilities include those actively traded on exchanges.

- Level 2 – inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques (e.g. the Black-Scholes model) for which all significant inputs are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Where applicable, these models project future cash flows and discount the future amounts to a present value using market-based observable inputs including interest rate curves, credit spreads, foreign exchange rates, and forward and spot prices for currencies. Our Level 2 investments primarily include corporate notes and bonds, foreign government bonds, mortgage- and asset-backed securities, commercial paper, certificates of deposit, and U.S. agency securities. Our Level 2 derivative assets and liabilities primarily include certain over-the-counter option and swap contracts.
- Level 3 – inputs are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques, including option pricing models and discounted cash flow models. Our Level 3 assets and liabilities primarily include investments in corporate notes and bonds, and goodwill and intangible assets, when they are recorded at fair value due to an impairment charge. Unobservable inputs used in the models are significant to the fair values of the assets and liabilities.

We measure equity investments without readily determinable fair values on a nonrecurring basis. The fair values of these investments are determined based on valuation techniques using the best information available, and may include quoted market prices, market comparables, and discounted cash flow projections.

Our other current financial assets and current financial liabilities have fair values that approximate their carrying values.

Contract Balances

As of September 30, 2018 and June 30, 2018, long-term accounts receivable, net of allowance for doubtful accounts, were $1.8 billion and $1.8 billion, respectively, and are included in other long-term assets on our consolidated balance sheets.

Recent Accounting Guidance

Recently Adopted Accounting Guidance

Income Taxes – Intra-Entity Asset Transfers

In October 2016, the Financial Accounting Standards Board ("FASB") issued new guidance requiring an entity to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs, rather than when the asset has been sold to an outside party. We adopted the guidance effective July 1, 2018. Adoption of the guidance was applied using a modified retrospective approach through a cumulative-effect adjustment to retained earnings as of the effective date. We recorded a net cumulative-effect adjustment that resulted in an increase in retained earnings of $557 million, which reversed the previous deferral of income tax consequences and recorded new deferred tax assets from intra-entity transfers involving assets other than inventory, partially offset by a U.S. deferred tax liability related to global intangible low-taxed income ("GILTI"). Adoption of the standard resulted in an increase in long-term deferred tax assets of $2.8 billion, an increase in long-term deferred tax liabilities of $2.1 billion, and a reduction in other current assets of $152 million. As a result of the Tax Cuts and Jobs Act ("TCJA"), we are continuing to evaluate the impact of this standard on our consolidated financial statements, including accounting policies, processes, and systems. Adoption of the standard had no impact to cash from or used in operating, financing, or investing on our consolidated cash flows statements.

Financial Instruments – Recognition, Measurement, Presentation, and Disclosure

In January 2016, the FASB issued a new standard related to certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. Most prominent among the changes in the standard is the requirement for changes in the fair value of our equity investments, with certain exceptions, to be recognized through net income rather than OCI.

We adopted the standard effective July 1, 2018. Adoption of the standard was applied using a modified retrospective approach through a cumulative-effect adjustment from accumulated other comprehensive income (“AOCI”) to retained earnings as of the effective date, and we elected to measure equity investments without readily determinable fair values at cost with adjustments for observable changes in price or impairments. The cumulative-effect adjustment included any previously held unrealized gains and losses held in AOCI related to our equity investments carried at fair value as well as the impact of recording the fair value of certain equity investments carried at cost. The impact on our consolidated balance sheets upon adoption was not material. Adoption of the standard had no impact to cash from or used in operating, financing, or investing on our consolidated cash flows statements.

Recent Accounting Guidance Not Yet Adopted

Financial Instruments – Targeted Improvements to Accounting for Hedging Activities

In August 2017, the FASB issued new guidance related to accounting for hedging activities. This guidance expands strategies that qualify for hedge accounting, changes how many hedging relationships are presented in the financial statements, and simplifies the application of hedge accounting in certain situations. The standard will be effective for us beginning July 1, 2019, with early adoption permitted for any interim or annual period before the effective date. Adoption of the standard will be applied using a modified retrospective approach through a cumulative-effect adjustment to retained earnings as of the effective date. We are currently evaluating the impact of this standard on our consolidated financial statements, including accounting policies, processes, and systems.

Financial Instruments – Credit Losses

In June 2016, the FASB issued a new standard to replace the incurred loss impairment methodology under current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. We will be required to use a forward-looking expected credit loss model for accounts receivables, loans, and other financial instruments. Credit losses relating to available-for-sale debt securities will also be recorded through an allowance for credit losses rather than as a reduction in the amortized cost basis of the securities. The standard will be effective for us beginning July 1, 2020, with early adoption permitted beginning July 1, 2019. Adoption of the standard will be applied using a modified retrospective approach through a cumulative-effect adjustment to retained earnings as of the effective date to align our credit loss methodology with the new standard. We are currently evaluating the impact of this standard on our consolidated financial statements, including accounting policies, processes, and systems.

NOTE 2 — EARNINGS PER SHARE

Basic earnings per share (“EPS”) is computed based on the weighted average number of shares of common stock outstanding during the period. Diluted EPS is computed based on the weighted average number of shares of common stock plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method. Dilutive potential common shares include outstanding stock options and stock awards.

The components of basic and diluted EPS were as follows:

(In millions, except per share amounts)

Three Months Ended September 30,	2018	2017
Net income available for common shareholders (A)	$8,824	$6,576
Weighted average outstanding shares of common stock (B)	7,673	7,708
Dilutive effect of stock-based awards	93	91
Common stock and common stock equivalents (C)	7,766	7,799
Earnings Per Share		
Basic (A/B)	$1.15	$0.85
Diluted (A/C)	$1.14	$0.84

Anti-dilutive stock-based awards excluded from the calculations of diluted EPS were immaterial during the periods presented.

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NOTE 3 — OTHER INCOME (EXPENSE), NET

The components of other income (expense), net were as follows:

(In millions)

Three Months Ended September 30,	2018	2017
Interest and dividends income	$681	$473
Interest expense	(674)	(672)
Net recognized gains on investments	243	573
Net losses on derivatives	(3)	(50)
Net gains (losses) on foreign currency remeasurements	5	(9)
Other, net	14	(39)
Total	$266	$276

Net Recognized Gains (Losses) on Investments

Net recognized gains (losses) on debt investments were as follows:

(In millions)

Three Months Ended September 30,	2018	2017
Realized gains from sales of available-for-sale securities	$ 7	$ 13
Realized losses from sales of available-for-sale securities	(85)	(80)
Other-than-temporary impairments of investments	0	(1)
Total	$(78)	$(68)

Net recognized gains (losses) on equity investments were as follows:

(In millions)

Three Months Ended September 30,	2018	2017
Net realized gains on investments sold	$203	$646
Net unrealized gains on investments still held	118	0
Other-than-temporary impairments of investments	0	(5)
Total	$321	$641

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NOTE 4 — INVESTMENTS

Investment Components

The components of investments were as follows:

(In millions)	Fair Value Level	Cost Basis	Unrealized Gains	Unrealized Losses	Recorded Basis	Cash and Cash Equivalents	Short-term Investments	Equity Investments
September 30, 2018								
Changes in Fair Value Recorded in Other Comprehensive Income								
Commercial paper	Level 2	$ 2,883	$ 0	$ 0	$ 2,883	$ 2,784	$ 99	$ 0
Certificates of deposit	Level 2	2,537	0	0	2,537	2,081	456	0
U.S. government securities	Level 1	111,281	9	(1,442)	109,848	4,419	105,429	0
U.S. agency securities	Level 2	639	0	0	639	349	290	0
Foreign government bonds	Level 2	4,981	1	(12)	4,970	1,384	3,586	0
Mortgage- and asset-backed securities	Level 2	3,358	4	(14)	3,348	0	3,348	0
Corporate notes and bonds	Level 2	7,143	22	(53)	7,112	0	7,112	0
Corporate notes and bonds	Level 3	15	0	0	15	0	15	0
Municipal securities	Level 2	268	32	(1)	299	0	299	0
Total debt investments		$ 133,105	$ 68	$ (1,522)	$ 131,651	$ 11,017	$ 120,634	$ 0
Changes in Fair Value Recorded in Net Income								
Equity investments	Level 1				$ 562	$ 239	$ 0	$ 323
Equity investments	Other				1,711	0	0	1,711

Total equity investments	$2,273	$ 239	$ 0	$ 2,034
Cash	$3,881	$ 3,881	$ 0	$ 0
Derivatives, net [a]	109	0	109	0
Total	$137,914	$ 15,137	$ 120,743	$ 2,034

(a) Refer to Note 5 – Derivatives for further information on the fair value of our derivative instruments.

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(In millions)	Fair Value Level	Cost Basis	Unrealized Gains	Unrealized Losses	Recorded Basis	Cash and Cash Equivalents	Short-term Investments	Equity Investments
June 30, 2018								
Changes in Fair Value Recorded in								
Other Comprehensive Income								
Commercial paper	Level 2	$ 2,513	$ 0	$ 0	$ 2,513	$ 2,215	$ 298	$ 0
Certificates of deposit	Level 2	2,058	0	0	2,058	1,865	193	0
U.S. government securities	Level 1	108,120	62	(1,167)	107,015	2,280	104,735	0
U.S. agency securities	Level 2	1,742	0	0	1,742	1,398	344	0
Foreign government bonds	Level 1	22	0	0	22	0	22	0
Foreign government bonds	Level 2	5,063	1	(10)	5,054	0	5,054	0
Mortgage- and asset-backed securities	Level 2	3,864	4	(13)	3,855	0	3,855	0
Corporate notes and bonds	Level 2	6,929	21	(56)	6,894	0	6,894	0
Corporate notes and bonds	Level 3	15	0	0	15	0	15	0
Municipal securities	Level 2	271	37	(1)	307	0	307	0
Total debt investments		$ 130,597	$ 125	$ (1,247)	$ 129,475	$ 7,758	$ 121,717	$ 0
Equity investments	Level 1				$ 533	$ 246	$ 0	$ 287
Equity investments	Level 3				18	0	0	18
Equity investments	Other				1,558	0	1	1,557
Total equity investments					$ 2,109	$ 246	$ 1	$ 1,862
Cash					$ 3,942	$ 3,942	$ 0	$ 0
Derivatives, net [(a)]					104	0	104	0
Total					$ 135,630	$ 11,946	$ 121,822	$ 1,862

(a) Refer to Note 5 – Derivatives for further information on the fair value of our derivative instruments.
Equity investments presented as "Other" in the tables above include investments without readily determinable fair values measured using the equity method or measured at cost with adjustments for observable changes in price or impairments, and investments measured at fair value using net asset value as a practical expedient which are not categorized in the fair value hierarchy. As of September 30, 2018 and June 30, 2018, equity investments without readily determinable fair values measured at cost with adjustments for observable changes in price or impairments were $820 million and $697 million, respectively.

As of September 30, 2018, we had no collateral received under agreements for loaned securities. As of June 30, 2018, collateral received under agreements for loaned securities was $1.8 billion and primarily comprised U.S. government and agency securities.

Unrealized Losses on Debt Investments

Debt investments with continuous unrealized losses for less than 12 months and 12 months or greater and their related fair values were as follows:

	Less than 12 Months		12 Months or Greater			
(In millions)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Total Fair Value	Total Unrealized Losses
September 30, 2018						
U.S. government and agency securities	$65,155	$(960)	$27,736	$(482)	$92,891	$(1,442)
Foreign government bonds	3,160	(8)	26	(4)	3,186	(12)
Mortgage- and asset-backed securities	1,130	(8)	145	(6)	1,275	(14)
Corporate notes and bonds	2,892	(37)	338	(16)	3,230	(53)
Municipal securities	42	(1)	0	0	42	(1)
Total	$72,379	$ (1,014)	$ 28,245	$ (508)	$ 100,624	$ (1,522)

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	Less than 12 Months		12 Months or Greater			
(In millions)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Total Fair Value	Total Unrealized Losses
June 30, 2018						
U.S. government and agency securities	$82,352	$(1,064)	$4,459	$(103)	$86,811	$(1,167)
Foreign government bonds	3,457	(7)	13	(3)	3,470	(10)
Mortgage- and asset-backed securities	2,072	(9)	96	(4)	2,168	(13)
Corporate notes and bonds	3,111	(43)	301	(13)	3,412	(56)
Municipal securities	45	(1)	0	0	45	(1)
Total	$91,037	$ (1,124)	$ 4,869	$ (123)	$ 95,906	$ (1,247)

Unrealized losses from fixed-income securities are primarily attributable to changes in interest rates. Management does not believe any remaining unrealized losses represent other-than-temporary impairments based on our evaluation of available evidence.

Debt Investment Maturities

(In millions)	Cost Basis	Estimated Fair Value
September 30, 2018		
Due in one year or less	$36,769	$36,577
Due after one year through five years	69,379	68,747
Due after five years through 10 years	26,053	25,444
Due after 10 years	904	883
Total	$ 133,105	$ 131,651

NOTE 5 — DERIVATIVES

We use derivative instruments to manage risks related to foreign currencies, equity prices, interest rates, and credit; to enhance investment returns; and to facilitate portfolio diversification. Our objectives for holding derivatives include reducing, eliminating, and efficiently managing the economic impact of these exposures as effectively as possible. Our derivative programs include strategies that both qualify and do not qualify for hedge accounting treatment.

Foreign Currency

Certain forecasted transactions, assets, and liabilities are exposed to foreign currency risk. We monitor our foreign currency exposures daily to maximize the economic effectiveness of our foreign currency hedge positions. Option and forward contracts are used to hedge a portion of forecasted international revenue and are designated as cash flow hedging instruments. Principal currencies hedged include the euro, Japanese yen, British pound, Canadian dollar, and Australian dollar.

Foreign currency risks related to certain non-U.S. dollar denominated securities are hedged using foreign exchange forward contracts that are designated as fair value hedging instruments.

Certain options and forwards not designated as hedging instruments are also used to manage the variability in foreign exchange rates on certain balance sheet amounts and to manage other foreign currency exposures.

Equity

Securities held in our equity investments portfolio are subject to market price risk. Market price risk is managed relative to broad-based global and domestic equity indices using certain convertible preferred investments, options, futures, and swap contracts not designated as hedging instruments. In the past, to hedge our price risk, we also used and designated equity derivatives as hedging instruments, including puts, calls, swaps, and forwards.

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Other

Interest Rate

Securities held in our fixed-income portfolio are subject to different interest rate risks based on their maturities. We manage the average maturity of our fixed-income portfolio to achieve economic returns that correlate to certain broad-based fixed-income indices using exchange-traded option and futures contracts, and over-the-counter swap and option contracts, none of which are designated as hedging instruments.

In addition, we use “To Be Announced” forward purchase commitments of mortgage-backed assets to gain exposure to agency mortgage-backed securities. These meet the definition of a derivative instrument in cases where physical delivery of the assets is not taken at the earliest available delivery date.

Credit

Our fixed-income portfolio is diversified and consists primarily of investment-grade securities. We use credit default swap contracts, not designated as hedging instruments, to manage credit exposures relative to broad-based indices and to facilitate portfolio diversification. We use credit default swaps as they are a low-cost method of managing exposure to individual credit risks or groups of credit risks.

Credit-Risk-Related Contingent Features

Certain of our counterparty agreements for derivative instruments contain provisions that require our issued and outstanding long-term unsecured debt to maintain an investment grade credit rating and require us to maintain minimum liquidity of $1.0 billion. To the extent we fail to meet these requirements, we will be required to post collateral, similar to the standard convention related to over-the-counter derivatives. As of September 30, 2018, our long-term unsecured debt rating was AAA, and cash investments were in excess of $1.0 billion. As a result, no collateral was required to be posted.

The following table presents the notional amounts of our outstanding derivative instruments measured in U.S. dollar equivalents:

	September 30,	June 30,
(In millions)	2018	2018
Designated as Hedging Instruments		
Foreign exchange contracts sold	$ 9,736	$11,101
Not Designated as Hedging Instruments		

Foreign exchange contracts purchased	11,056	9,425
Foreign exchange contracts sold	9,600	13,374
Equity contracts purchased	40	49
Equity contracts sold	7	5
Other contracts purchased	1,000	878
Other contracts sold	512	472

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Fair Values of Derivative Instruments

The following table presents our derivative instruments:

(In millions)	Derivative Assets	Derivative Liabilities	Derivative Assets	Derivative Liabilities
	September 30, 2018		June 30, 2018	
Changes in Fair Value Recorded in Other Comprehensive Income				
Designated as Hedging Instruments				
Foreign exchange contracts	$151	$0	$174	$ 0
Changes in Fair Value Recorded in Net Income				
Designated as Hedging Instruments				
Foreign exchange contracts	97	0	95	0
Not Designated as Hedging Instruments				
Foreign exchange contracts	129	(118)	256	(197)
Equity contracts	5	(3)	2	(7)
Other contracts	9	(8)	11	(3)
Gross amounts of derivatives	391	(129)	538	(207)
Gross amounts of derivatives offset in the balance sheet	(101)	100	(152)	153
Cash collateral received	0	(168)	0	(235)
Net amounts of derivatives	$290	$(197)	$386	$ (289)

Reported as

Short-term investments	$109	$0	$104	$ 0
Other current assets	161	0	260	0
Other long-term assets	20	0	22	0
Other current liabilities	0	(194)		